What Lurks Beneath US Nonfarm Payrolls Is Not Encouraging

- **Headline job growth missed expectations…**
- **...as education sector jobs fell**
- **There was job destruction excluding call backs of furloughed workers**
- **The number of permanently laid off continues to rise**

US nonfarm payrolls m/m change 000s / UR (%) / wage growth y/y (%), SA, September:
Actual: 661 / 7.9 / 4.7
Scotia: 1000 / 8.0 / 4.8
Consensus: 859 / 8.2 / 4.8
Prior: 1489 / 8.4 / 4.6 (revised from 1371 / 8.4 / 4.7)

A gain of 661,000 jobs is nothing to shake a stick at, but there are two reasons why it's generally disappointing. Market participants should be increasing the odds of resuming very weak or negative payroll numbers. This is not a certainty but it would require a rapid change in favour of organic job growth. The initial market reaction was muted as more of the focus remains on Trump's diagnosis, US stimulus talks and Brexit headlines.

First, take callback effects out of the picture and there was net job destruction. As chart 1 demonstrates, the number of unemployed folks on temporary lay off and brought back on payroll fell by 1.52 million to 4.64 million. In one sense this is welcome because it takes the number of furloughed workers down from a peak of 18.1 million to 4.2 million which is encouraging. This figure could continue to decline to the pre-covid level of about 750k but the issue is whether they all get called back or just get converted to permanent layoffs and whether they give up searching for work.

In another sense, however, excluding this effect from the headline means jobs excluding call backs fell by 859k. That indicates net job destruction, or the inability of the US economy to generate organic job growth. This will become a more important factor going forward as the number of furloughed workers continues to decline if organic job growth does not pick up. It amplifies the risk of renewed net job losses.

You can see this in terms of the rising number of outright job losses in the US. Permanently laid off workers not expected to be called back continues to rise (chart 2). That figure is now at its highest since November 2013. It's not done climbing yet but remains well shy of the GFC peak of 8.3 million. As another indication of the issue at hand, note the growing wedge in chart 1 between what is happening to aggregate payrolls versus the temporarily laid off which confirms that ex-callback jobs are being lost.

The average duration of unemployment is climbing and is at 20.7 weeks now, but that restores it to where it was pre-covid. This is a distortion as people left the workforce initially. Now that this has stabilized, the real test begins in terms of duration of unemployment.

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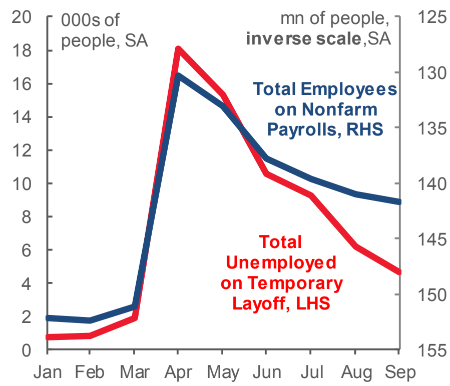
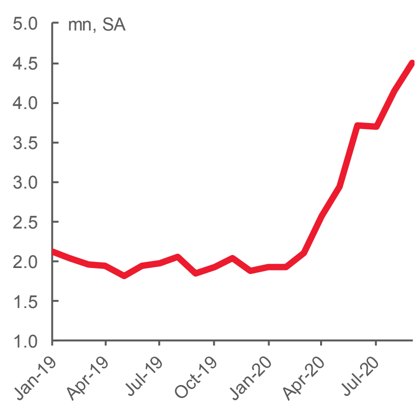
Chart 1

Temporarily Laid Off US Employees Continue to Return to Work



Sources: Scotiabank Economics, US BLS.

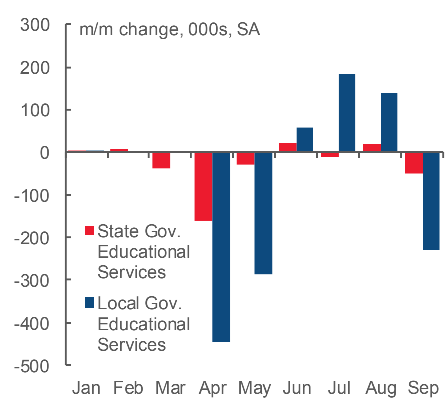
Chart 2 **Permanent US Layoffs**



Sources: Scotiabank Economics, US BLS.

Chart 3

Fewer Teachers Return to Work as New School Year Resumes



Sources: Scotiabank Economics, US BLS.

The second reason why the report is disappointing is that the main reason why the 661k figure fell shy of expectations had to do with job destruction in the education sector (chart 3). Education sector jobs at local governments fell by 231k while they fell by 49k at state governments for a combined hit of 280k. The case for removing this effect from the headline miss is that it is a narrow distortion that masks what is going on in the underlying private sector. The case for not removing this hit is that a job is a job and these are generally good jobs we're talking about. I lean toward the latter interpretation in terms of not fading the headline miss as the lingering impact of covid-19 continues.

Why did this education sector hit occur? One possible argument is the hit to state and local government finances in the absence of further stimulus from Washington. Another possible reason is that teachers and other education sector workers were reticent to return to work in the midst of the pandemic. A third reason is that fewer of them were needed as schools shifted toward more on-line content.

The Federal government also shed 34k workers. Overall, the public sector dropped 216,000 jobs with the only offsetting bright spot being that local governments added 96k jobs outside of education. This, in turn, might suggest that the issue is less about local government finances than it is about the other factors influencing education sector jobs.

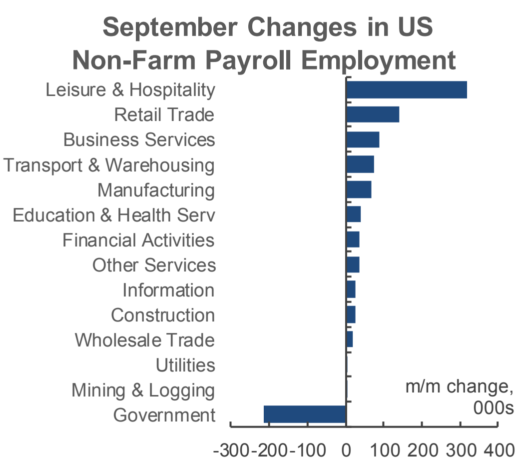
There was otherwise decent breadth across the sectors as shown in chart 4. Goods sector employment was up by 93k with services up 784k. Within goods, there was a 66k rise in manufacturing employment and a 26k rise in construction jobs. Within services, leisure/hospitality was up 318k, retail was up 142k, and other trade/transport up 95k.

Hours worked came in strong at 1.1% m/m on the callback effect.

The unemployment rate declined to 7.9% from 8.4% mainly because people left the workforce (chart 5). It is derived from the companion household survey which showed job growth at 275k but a 695k shrinkage in the size of the labour force. The participation rate fell three tenths to 61.4%.

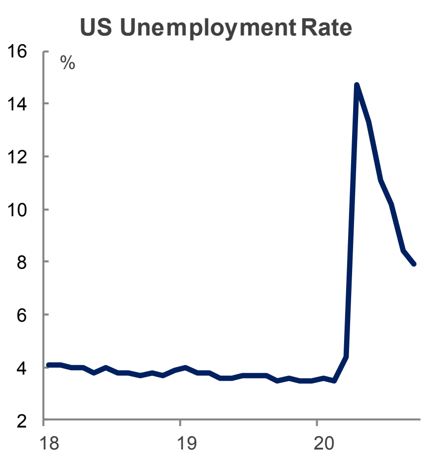
Wage growth was in line with expectations at 0.1% m/m and 4.7% y/y (chart 6). It remains high because of the ongoing pandemic distortion that resulted in a disproportionate hit to the jobs of lower than average wage workers. Thus, 5% wage growth is not to be treated as a good sign.

Chart 4



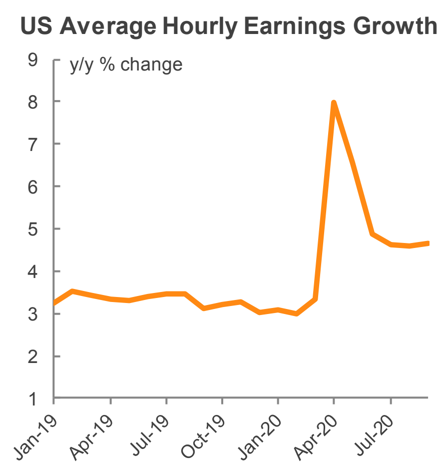
Sources: Scotiabank Economics, US BLS.

Chart 5



Sources: Scotiabank Economics, BLS.

Chart 6



Sources: Scotiabank Economics, BLS.